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BEFORE THE
DEPARTMENT OF TRANSPORTATION
WASHINGTON, D.C.

DEPARTMENT OF TRANSPORTATION

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DOCKET SECTION

Motion of

UNITED AIR LINES, INC.

for an order instituting an investigation and
inviting comments

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Docket OST-96-1850 - 4

ANSWER OF
CONTINENTAL AIRLINES, INC.

Communications with respect to
this document should be sent to:

Rebecca G. Cox
Vice President, Government Affairs
CONTINENTAL AIRLINES, INC.
1300 I Street, N.W.
Suite 950 East
Washington, D.C. 20005

and

R. Bruce Keiner, Jr.
Calvin Davison
CROWELL & MORING LLP
1001 Pennsylvania Avenue, N.W.
Washington, D.C. 20004-2595
(202) 624-2615

Counsel for
Continental Airlines, Inc.

October 21, 1996

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ANSWER OF
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United¹ has asked the Department to "issue an order instituting an investigation gathering the necessary data and inviting comments from all interested parties on the proposal" of American and British Airways "to form a global alliance." The critical U.S.-U.K. issue, as Continental has maintained from the beginning, is access to Heathrow. Until that issue is resolved, the U.S. should neither negotiate an "open skies" agreement which would be meaningless without Heathrow access nor investigate an American/British Airways alliance which cannot be seriously considered, much less approved, without substantial new Heathrow access for U.S. carriers such as Continental. Continental agrees with

¹ Common names of carriers are used.

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United that neither U.K. authorities nor E.U. authorities will consider fully the interests of U.S. carriers and U.S. consumers, but it is premature to commence any investigation of an American/British Airways alliance prior to securing access for other carriers to London's Heathrow airport sufficient to assure meaningful competition for any such alliance. As final arbiter of approval and antitrust immunity, the Department will have before it the views of the U.S. Department of Justice as well as the views of the U.K. and E.U. authorities when it investigates any alliance proposed by American and British Airways. To conduct a meaningful evaluation, the Department must have a complete picture of the slots, terminal access and route rights available at Heathrow to ameliorate the anticompetitive effects of combining the two primary U.S.-U.K. carriers and know how U.S. carriers such as Continental will use their new access. As explained below, Continental itself can bring effective new competition to the U.S.-London market by operating six daily Newark-Heathrow flights, three daily Houston-Heathrow flights and one daily Cleveland-Heathrow flight as well as maintaining the Newark/Houston-London (Gatwick) service it provides today.

Continental states as follows in support of its position.

1. While various agencies in the U.K. and the E.U. as well as the U.S. Department of Justice are currently reviewing the potential combination of American and British Airways, the only possible conclusion to these investigations

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must be that the combination would be extraordinarily anticompetitive unless other airlines are given access to Heathrow which allows them to compete effectively with the American/British Airways alliance. No DOT investigation is required to confirm that conclusion. As DOT Deputy Assistant Secretary Murphy said this past summer, ". . . even for us to begin to consider an alliance which includes antitrust immunity will absolutely require a full 'open skies' agreement and more" since "[a]ll of our carriers who will have to compete with a British Airways' alliance will have to be in place and operating at Heathrow in order to discipline a new alliance."² Instead of instituting a voluminous and time-consuming investigation which may prove fruitless if sufficient access at Heathrow is not forthcoming, the Departments of Transportation and State are ascertaining through diplomatic channels what Heathrow access and what route rights will be available when and if American and British Airways seek approval and antitrust immunity in the U.S. for their alliance.³ Any meaningful investigation of the proposed alliance must consider the reality of access to U.K. routes and, most importantly, the scope of the access to slots and facilities at Heathrow. At present, no access at Heathrow is available to Continental or other U.S. carriers

² Speech of Patrick V. Murphy Before the 68th Annual American Association of Airport Executives Annual Conference and Exposition at Las Vegas, Nevada, June 11, 1996 at 20.

³ Until effective access at Heathrow is assured, further negotiations on fifth-freedom rights, pricing regimes, dispute resolution, inward investment, Fly America and other liberalization issues are meaningless.

not already serving Heathrow. Under these circumstances, the Department would be required to reject the American/British Airways proposal out of hand if it were submitted for approval or investigated today.

2. Continental has formulated plans for U.S.-London operations which would provide significant competition to an American/British Airways alliance at both Heathrow and Gatwick if sufficient Heathrow access is made available to Continental. Continental would operate six daily Heathrow flights serving Newark, three daily flights serving Houston and one daily flight serving Cleveland. (See Attachment A) Without Continental's Heathrow flights, an American/British Airways alliance would have a serious adverse impact upon competition as measured by the Hirschman-Herfindahl Index ("HHI"). (See Attachments B and C) Continental's new Heathrow flights would greatly reduce the adverse competitive impact of an American-British Airways alliance. The impact is most pronounced in New York/Newark but it is also substantial in Texas and the Midwest. For example, in New York/Newark-Heathrow the introduction of new Continental service from Newark would reduce the change in the HHI resulting from the American-British Airways alliance from nearly 2000 to under 700. (See Attachment B) In Texas-London the change in the HHI is reduced from a whopping 3700 to 817, still a large change but much less restrictive of competition with the addition of new Continental service between Houston Intercontinental and London Heathrow. (See Attachment C) Similarly, for service

between the Midwest and points east and London, the introduction of new Continental Cleveland service would reduce the change in the HHI from 1688 to 1055. (See Attachment C)

With six daily flights at Newark, Continental will be able to compete effectively with the American/British Airways alliance because only Continental has a true hub in the Newark/New York area capable of providing effective competition with such a dominant alliance. With nonstop service between Newark and 86 destinations today and new flights being added regularly, Continental will be able to offer multiple connecting opportunities each day for U.S.-London passengers using Continental's six daily Newark-Heathrow flights (see Attachment D), just as Continental will be offering multiple connecting opportunities for passengers using its six daily Newark-Los Angeles flights.

Three daily flights between Heathrow and Continental's Houston hub would permit Continental to compete effectively with an American/British Airways alliance at Dallas/Ft. Worth and throughout the catchment areas served through the two Texas hubs. With service between Houston and 100 cities on Continental and Continental Express (see Attachment E), Continental will be able to offer daily connecting options between London and points served through Houston, competing with the incumbent Heathrow carriers.

Instituting Cleveland-Heathrow service would introduce the only nonstop transatlantic service at Cleveland, offer competitive interline connecting service at

Heathrow and provide important additional competition with the American and United mega-hubs at Chicago for passengers and shippers throughout the midwest parts of the east, and the west. (See Attachment F)

Continental has developed specific schedules for these new Houston, Newark and Cleveland-Heathrow services (see Attachment A), and it is planning to use both the seven DC-10 aircraft Continental already has on order for delivery in the first quarter of 1997 and additional aircraft Continental is now seeking to provide additional Heathrow services. In addition to providing the 10 new daily round trip flights serving Heathrow, Continental will continue to offer the Newark and Houston- London (Gatwick) service it provides today, assuring effective competition for American/British Airways and other carriers on both the U.S.-Heathrow and U.S.-Gatwick routes.

3. Securing Heathrow access for Continental as part of an overall U.S.-U.K. accommodation should not be difficult. The U.K. Transport Select Committee of the House of Commons has noted that Continental's request for 20-well-timed Heathrow slots is a "modest" request which "could be accommodated by . . . incremental increases in slot capacity" to "help competition." If sufficient slots are unavailable through capacity increases, the Transport Select Committee concluded that "effective competitive access to Heathrow may require the alliance to yield up,

either by divestment or exchange, some desirable slots."⁴ Nonetheless, until the Department is certain that such access will be granted it should not institute any proceedings to consider a proposed American/British Airways alliance. Without satisfactory new entry for U.S. carriers at Heathrow, the American/British Airways alliance is so clearly anticompetitive it should receive no consideration by the Department, much less consideration for antitrust immunity.

4. The advantages of Heathrow over other London airports are well established. Passengers traveling to and from the London area prefer Heathrow because of its greater convenience. Heathrow is particularly desired by connecting passengers because of the much greater connecting opportunities there to all areas of the world. For every business traveler at Gatwick, there are seven at Heathrow. Twice as many destinations have connecting service at Heathrow compared to Gatwick, and 78 third country airlines provide connecting service beyond Heathrow compared to 34 beyond Gatwick, where British Airways dominates the connections. Heathrow captures 70% of the total London traffic, and American and British Airways reportedly hold some 80% of the prime-time transatlantic slots at Heathrow, ensuring the success of their alliance.

5. Access to Heathrow is particularly important for Continental. In addition to providing essential competition to an American/British Airways

⁴ Transport Committee, Sixth Report, "The Proposed Alliance Between British Airways and American Airlines," July 30, 1996.

alliance, Continental needs Heathrow access from its gateways to help restore its competitive position in the United Kingdom market. This access will enable it to provide more effective service for local passengers seeking access to Heathrow, their preferred airport, and expand connecting opportunities available to Continental's passengers at London. Heathrow access for Continental will help redress the competitive disadvantage suffered by Continental because of the Heathrow access of its competitors, American, United, British Airways, and Delta/Virgin Atlantic, all of which, except American, provide nonstop service between Heathrow and Newark. Without Heathrow access, Continental also will suffer a competitive disadvantage against those competitors in the U.S.-U.K. market whose alliance partners, such as Delta/Sabena/Swissair/Austrian, Northwest/KLM and United/Lufthansa/SAS, already have Heathrow authority, since the U.S. partners will be able to start new services as soon as their alliance partners agree to using the existing Heathrow slots and facilities for their joint transatlantic service as well as competing jointly for U.S.-Europe traffic through other European hubs. Indeed, Continental understands that United has leased Heathrow slots to its own global alliance partner, Lufthansa. In fact, with SAS a 40% shareholder in British Midland (the second largest slot holder at Heathrow) and KLM a 45% shareholder in Air UK (with 26 weekly roundtrip flights at Heathrow and a new concentration on service at Stansted) the antitrust-immunized alliances will have even more potential slots available to them. In

contrast, although Continental hopes to have an alliance with Air France, no antitrust immunity is being sought, the alliance will not apply to U.K. markets, and Continental will be competing with Air France as well as its other alliance partner, Delta.⁵

6. If the American and British Airways alliance is approved, that alliance will not only dominate the New York/Newark-London market but have a strong competitive advantage from its access to Heathrow slots and facilities. Continental has the only true hub in the New York area and, therefore, can offer significant public benefits providing service between Heathrow and Newark. The U.S. has lost market share in the New York/Newark-London market because no hub carrier has Heathrow rights, and United has been an ineffective competitor forced to reduce both its schedules and aircraft size as well as leasing out Heathrow slots.⁶ Only expanded Newark-U.K. access for Continental at London, with six daily flights at Heathrow, can provide competition for the American/British Airways alliance at New York/Newark. Continental needs a minimum of six daily Heathrow frequencies to compete with American and British Airways because they presently operate 15 daily frequencies in the New

⁵ Similarly, Continental's code-share arrangements with Alitalia and CSA neither enjoy antitrust immunity for services via any European hub nor involve U.K. service.

⁶ In contrast, Continental is flying 12 weekly Newark-London (Gatwick) flights, the maximum permitted under the U.S.-U.K. agreement.

York/Newark-London market. If their alliance is implemented, they plan an hourly "shuttle" schedule. See "BA and American Plan US Shuttle," The Times of London, July 25, 1996 at 20. To compete with such an American/British Airways shuttle, Continental requires at least six daily Newark-Heathrow flights, and additional frequencies will be required in the future as Continental is able to develop the market fully.

7. Access to Heathrow is far more important to Continental than it is to U.S. carriers which already have antitrust-immunized alliances with European carriers. Through its alliance with Lufthansa, United can provide effective competition between its U.S. gateways and points throughout the world via Frankfurt. Similarly, Delta's antitrust-immunized alliance with Sabena, Swissair and Austrian gives Delta broad access to points throughout Europe and the Middle East through Delta's own hub at Frankfurt and the hubs of its alliance partners in Brussels, Zurich and Vienna. Finally, Northwest's antitrust-immunized alliance with KLM provides worldwide access through KLM's Amsterdam hub. Both Delta and United have claimed that worldwide access through European hubs justified approval and antitrust immunity for their own alliances so they could compete effectively with other European alliances. Despite Delta's service at 11 cities through its Frankfurt hub, Delta and its alliance partners argued that they required approval and antitrust immunity "to compete more effectively against larger networks created by competing global alliances."

(See Order 96-5-26 at 7, n.11). Similarly, United and Lufthansa argued that "a fully implemented Alliance Agreement will enable United and Lufthansa to increase their competitiveness, placing additional commercial pressure on rival European carriers and carrier alliances." (See Order 96-5-12 at 7) Because carriers with antitrust-immunized alliances can share slots and facilities at Heathrow and coordinate their schedules and pricing both at Heathrow and at alternative European hubs, they can compete effectively with an American/British Airways alliance without securing the new slots and facilities Continental requires.

United suggests that slot constraints at JFK and Chicago must be addressed along with constraints at Heathrow and implies that additional Heathrow slots for United may be more important than additional slots for other U.S. carriers, but United already holds more Heathrow slots than it uses. United holds more slots than any other carrier at O'Hare. Although United cannot expect to secure sufficient JFK slots to develop a meaningful hub, Continental's service at Newark will offer effective competition for American/British Airways services at JFK immediately.

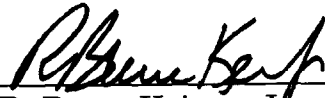
8. For the foregoing reasons, Continental urges the Department to defer any consideration of an American/British Airways alliance until competitive access to Heathrow is assured for Continental and the Department can balance the anticompetitive effects of a combination of the two largest carriers in the U.S.-U.K.

market against the pro-competitive effects of additional service by Continental at Heathrow.

Respectfully submitted,

CROWELL & MORING LLP

By:


R. Bruce Keiner, Jr.


Calvin Davison

Counsel for
Continental Airlines, Inc.

CERTIFICATE OF SERVICE

I certify that I have this date served a copy of the foregoing document on United and all parties served with United's motion in the manner specified in the Department's Rules of Practice.


Calvin Davison

October 21, 1996

Continental Airlines

Continental Heathrow Frequencies

<u>Market</u>	<u>Flt #</u>	<u>Eastbound</u>	<u>Flt #</u>	<u>Westbound</u>
EWR-LHR	CO-008	0945-2140	CO-001	0815-1100
	CO-006	1830-0625+1	CO-009	0915-1200
	CO-014	1900-0655+1	CO-003	1115-1400
	CO-002	2000-0755+1	CO-007	1230-1515
	CO-016	2030-0825+1	CO-015	1500-1745
	CO-012	2130-0925+1	CO-017	1800-2045
IAH-LHR	CO-022	1540-0645+1	CO-023	0900-1310
	CO-024	1840-0955+1	CO-027	1200-1610
	CO-026	2115-1220+1	CO-029	1450-1900
CLE-LHR	CO-032	2025-0840+1	CO-033	1055-1405

Service Between the United States and London Heathrow
Impact of AA/BA Alliance
With and Without Additional CO Service

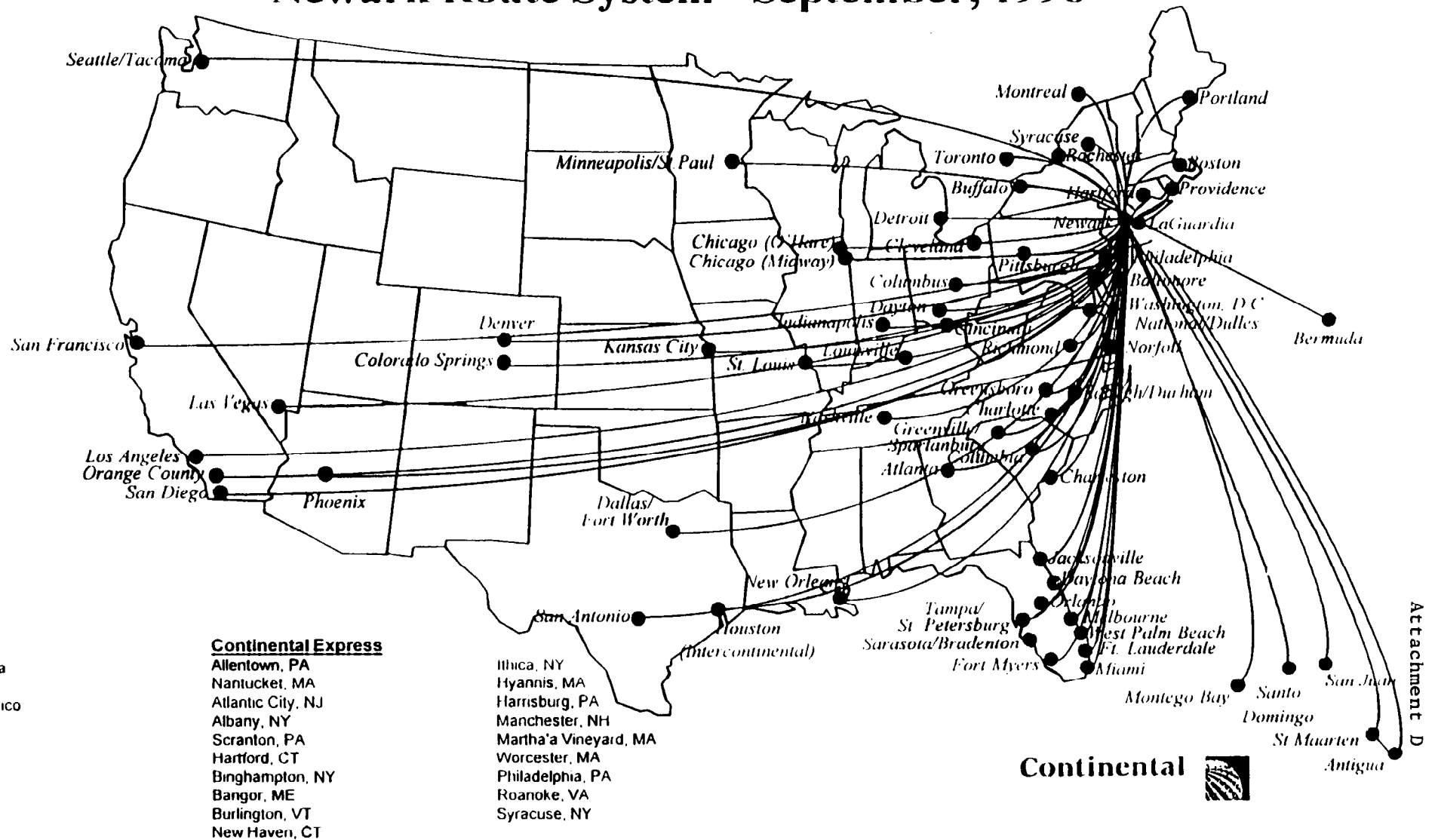
	Premerger HHI	Postmerger HHI		Change in HHI		Impact of Adds on HHI	AA/BA Combined Share		Impact of Adds on AA/BA Share
		W/O Adds	With Adds	W/O Adds	With Adds		W/O Adds	With Adds	
<u>Cities</u>									
New York	2738	4730	3436	1992	698	-1294	66%	53%	-13%
<u>Regions</u>									
Northeast	3287	5268	4126	1981	839	-1142	70%	61%	-9%
Mid-Atlantic	3364	5497	4350	2133	986	-1147	72%	63%	-9%
Midwest & East	3308	5817	4603	2509	1295	-1214	75%	65%	-10%
Rocky & East	3308	5817	4293	2509	985	-1524	75%	62%	-13%
<u>National</u>									
U.S.	3179	5218	4092	2039	913	-1126	70%	61%	-9%

Service Between the United States and London Heathrow & Gatwick
Impact of AA/BA Alliance
With and Without Additional CO Service

	Premerger HHI	Postmerger HHI		Change in HHI		Impact of Adds on HHI	AA/BA Combined Share		Impact of Adds on AA/BA Share
		W/O Adds	With Adds	W/O Adds	With Adds		W/O Adds	With Adds	
<u>Cities</u>									
New York	2693	4560	3487	1867	794	-1073	65%	53%	-12%
<u>States</u>									
Texas	4185	7885	5002	3700	817	-2883	75%	49%	-26%
<u>Regions</u>									
Northeast	3144	4886	3967	1742	823	-919	70%	59%	-11%
Mid-Atlantic	3090	4766	4020	1676	930	-746	72%	60%	-12%
Midwest & East	2616	4304	3671	1688	1055	-633	75%	58%	-17%
Rocky & East	2608	4363	3629	1755	1021	-734	75%	57%	-18%
<u>National</u>									
U.S.	2653	4263	3598	1610	945	-665	70%	57%	-13%

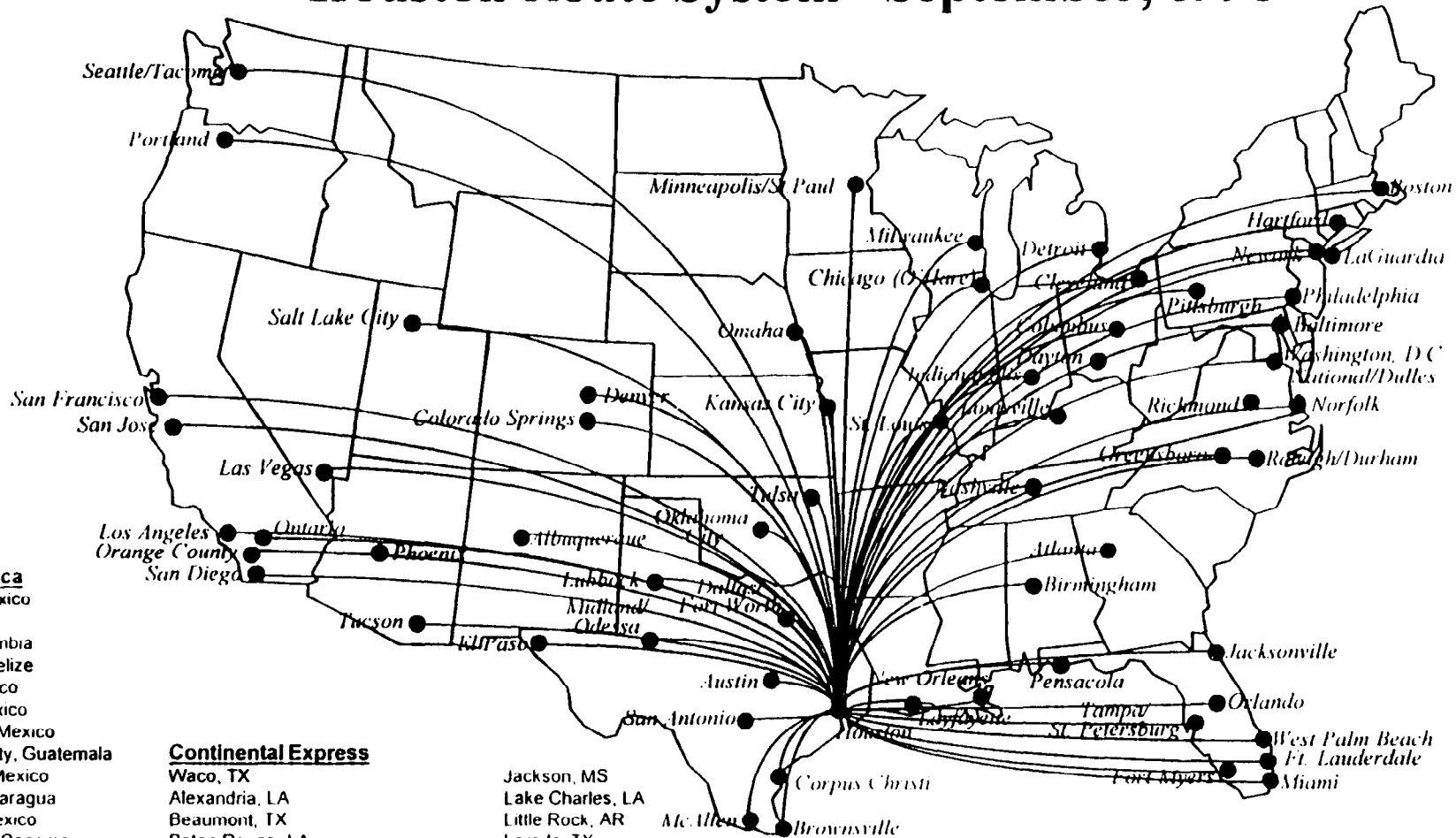
Continental Airlines, Inc.

Newark Route System - September, 1996



Continental Airlines, Inc.

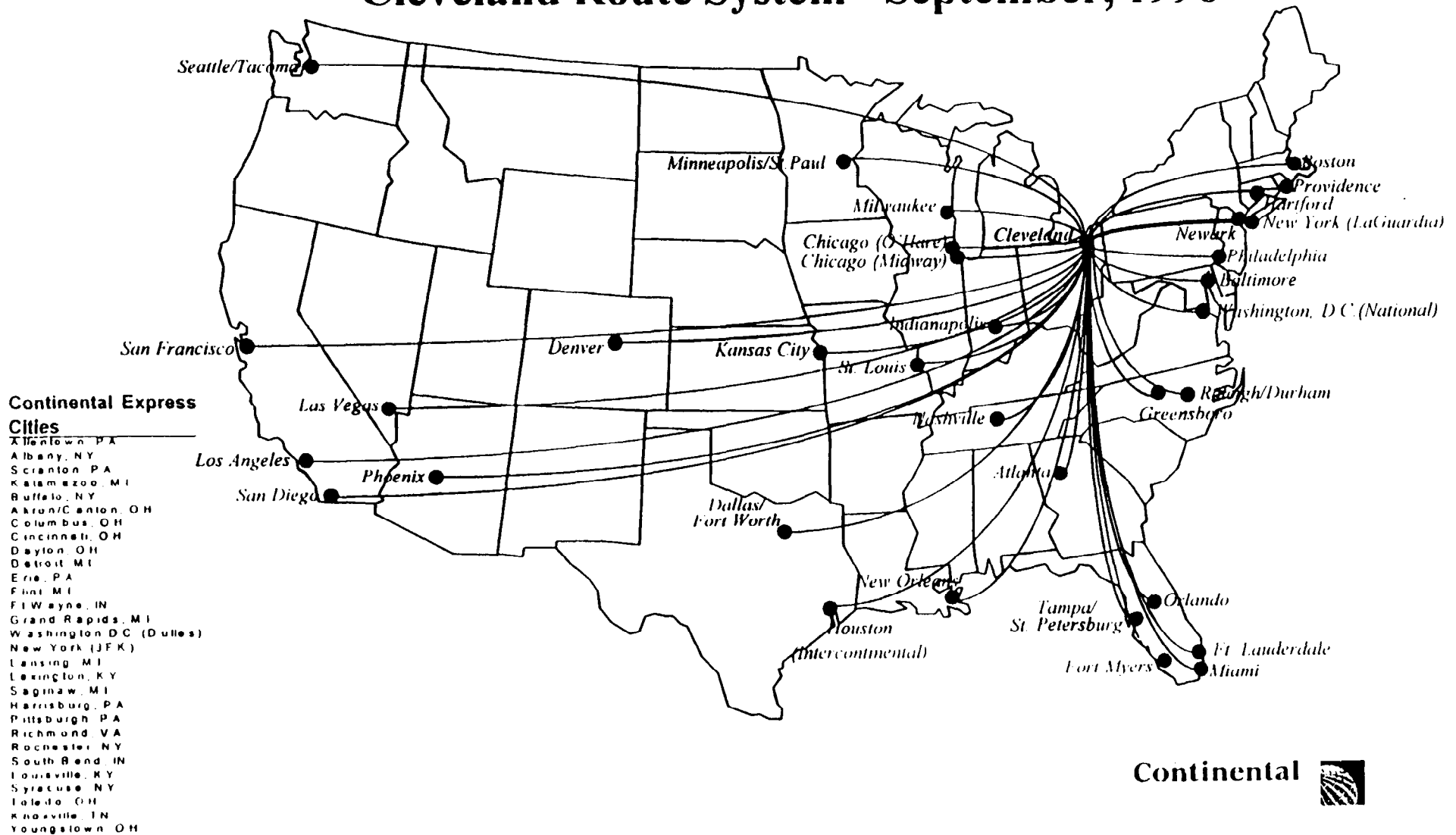
Houston Route System - September, 1996



Continental 

Continental Airlines, Inc.

Cleveland Route System - September, 1996



SERVICE LIST (Docket OST-96-1850)

October 21, 1996

Carl B. Nelson, Jr.
Associate General Counsel
American Airlines, Inc.
1101 17th Street, N.W.
Suite 600
Washington, D.C. 20036

Robert E. Cohn
Shaw, Pittman, Potts & Trowbridge
2300 N Street, N.W.
Washington, D.C. 20037
(for Delta)

Richard D. Mathias
Zuckert, Scoutt & Rasenberger, L.L.P.
888 Seventeenth Street, N.W.
Washington, DC 20006
(for USAir)

Joel Stephen Burton
Ginsburg, Feldman and Bress, Chartered
1250 Connecticut Avenue, N.W.
Suite 800
Washington, D.C. 20036
(for United)

Michael G. Whitaker
Director - International
and Regulatory Affairs
United Air Lines, Inc.
1707 L Street, N.W.
Suite 300
Washington, D.C. 20036

Megan Rae Poldy
Associate General Counsel
Northwest Airlines, Inc.
901 15th Street, N.W., Suite 310
Washington, D.C. 20005

Peter Kirk
British Embassy
Civil Aviation Section
3100 Massachusetts Avenue, N.W.
Washington, D.C. 20008

Tony Fortnam
British Airways
1850 K Street, N.W.
Suite 300
Washington, D.C. 20006

Richard J. Fahy, Jr.
Consulting Attorney
808 17th Street, NW, Suite 520
Washington, D.C. 20006
(for Trans World)

Robert M. Beckman
Bode & Beckman
1150 Connecticut Avenue, N.W.
Ninth Floor
Washington, D.C. 20036
(for Laker)

Brian T. Hunt
General Counsel
American Trans Air
7337 W. Washington St.
Indianapolis, IN 46231

Don Hainbach
Boros & Garofalo
1201 Connecticut Avenue, N.W.
Suite 700
Washington, D.C. 20036
(for British Airways)

Stephen L. Gelband
Hewes, Morella, Gelband & Lamberton
1001 Potomac Street, N.W.
Suite 300
Washington, D.C. 20007

Jeffrey N. Shane
Wilmer, Cutler & Pickering
2445 M Street, N.W.
Washington, DC 20037-1420
(for Virgin Atlantic)